

**UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF CALIFORNIA**

SECURITIES AND EXCHANGE
COMMISSION,

Plaintiff,

vs.

LOUIS SCHOOLER and FIRST
FINANCIAL PLANNING CORPORATION
d/b/a WESTERN FINANCIAL
PLANNING CORPORATION,

Defendants.

CASE NO. 12-CV-2164-LAB-JMA

**ORDER DENYING DEFENDANTS'
MOTION TO DISSOLVE
TEMPORARY RESTRAINING
ORDER**

The Court granted the SEC's *ex parte* motion for a temporary restraining order on September 6, 2012. According to the SEC, Defendants are violating the registration and antifraud provisions of the federal securities laws by, among other things, selling partnership interests in undeveloped land at a huge markup.

On September 11, Defendants filed an emergency motion to dissolve or modify the TRO pursuant to Fed. R. Civ. P. 65(b)(4). The motion makes, in essence, three arguments, which the Court summarized as follows in an order setting a briefing schedule that it entered the same day:

The first is that, by its own admission, the SEC didn't show that irreparable injury would result before Defendants could be heard. In fact, the SEC took the position, mistaken in Defendants' view, that "[u]nlike private litigants, if the government can show a probability of success on the merits, the courts presume irreparable injury in Commission enforcement actions where injunctive relief is sought." (Doc. No. 3-1 at 13.)

The Defendants' second argument cuts to the heart of the SEC's jurisdiction to bring claims against them: the general partnership investments at issue simply are not securities. Here, the Defendants take issue with the SEC's claim in its moving papers

that “[a]lthough some courts have found that investments in land solely for the purpose of obtaining profits from appreciation of property value on resale are not securities, and some general partnership interests are not investment contracts, the GP units at issue in this case are securities.” (Doc. No. 3-1 at 14.)

And the Defendants’ third argument is that the TRO threatens to do their business irreparable harm by its requirement that the appointed receiver notify each and every investor of the SEC’s allegations and the TRO itself. Related to this, the Defendants argue that the TRO places the receiver in the conflicted position of serving the General Partnerships alongside Western: “Wearing his hat as receiver to the General Partnerships, he is required to send out notices to all of Western’s investors. Wearing his hat as receiver to Western, it would be gross negligence or worse to send out a mass mailing to every past customer spreading inaccurate statements and allegations and would irreparably harm Western.” (Doc. No. 14 at 3.)

(Doc. No. 17 at 1–2.)

The SEC has now responded to Defendants’ arguments, and the Court will address them in sequence.

I. Irreparable Harm

A TRO is simply a preliminary injunction issued on short notice or no notice at all, and with a quick expiration date. The standards governing their issuance are “substantially identical.” *Stuhlbarg Int’l Sales Co. v. John D. Brush & Co.*, 240 F.3d 832, 839 n.7 (9th Cir. 2001). A plaintiff must show, among other things, that it “is likely to suffer irreparable harm in the absence of preliminary relief.” *Winter v. Natural Res. Def. Council, Inc.*, 555 U.S. 7, 20 (2008).

The TRO sought by the SEC, however, was issued without written notice to Defendants, and that requires a heightened showing of irreparable harm under Federal Rule of Civil Procedure 65:

(1) Issuing Without Notice. The court may issue a temporary restraining order without written or oral notice to the adverse party or its attorney only if:

(A) specific facts in an affidavit or a verified complaint clearly show that immediate and irreparable injury, loss, or damage will result to the movant before the adverse party can be heard in opposition; and

1 (B) the movant's attorney certifies in writing any efforts made to
 2 give notice and the reasons why it should not be required.

3 Fed. R. Civ. P. 65(b). In other words, while a standard-issue preliminary injunction must find
 4 a *likelihood* of irreparable harm, a secret-issue TRO must find a certainty of it. This higher
 5 hurdle "reflect[s] the fact that our entire jurisprudence runs counter to the notion of court
 6 action taken before reasonable notice and an opportunity to be heard has been granted both
 7 sides of a dispute." *Granny Goose Foods, Inc. v. Bhd. of Teamsters*, 415 U.S. 423, 438
 8 (1974).

9 Defendants accuse the SEC of "giv[ing] itself a pass on the irreparable injury
 10 requirement," and indeed it does. But it does so on good authority—and, critically, only with
 11 respect to the basic standard for issuance of a preliminary injunction or temporary restraining
 12 order, not with respect to the notice requirement. (See Doc. No. 3-1 at 12–13.) The SEC
 13 may obtain a preliminary injunction simply by establishing "(1) a *prima facie* case of previous
 14 violations of federal securities laws, and (2) a reasonable likelihood that the wrong will be
 15 repeated." *SEC v. Unique Fin. Concepts, Inc.*, 196 F.3d 1195, 1199 n.2 (11th Cir. 1999).
 16 The irreparable harm requirement is waived, as it were, because "[i]n statutory enforcement
 17 cases where the government has met the 'probability of success' prong of the preliminary
 18 injunction test . . . the passage of the statute is itself an implied finding by Congress that
 19 violations will harm the public," *United States v. Nutri-Cology, Inc.*, 982 F.2d 394, 398 (9th
 20 Cir. 1992). See also *SEC v. Mgmt. Dynamics, Inc.*, 515 F.2d 801, 808 (2d Cir. 1975) ("But
 21 the statutory imprimatur given SEC enforcement proceedings is sufficient to obviate the need
 22 for a finding of irreparable injury at least where the statutory prerequisite the likelihood of
 23 future violation of the securities laws has been clearly demonstrated.")

24 Contrary to the Defendants' argument, the SEC doesn't ignore Rule 65 or read into
 25 it the legal standard for issuance of a preliminary injunction discussed in *Unique Fin.*
 26 *Concepts*, *Nutri-Cology*, and *Mgmt. Dynamics*. The notice page of its TRO application
 27 explicitly "seeks waiver of the notice requirements of Rule 65(b)" on the ground that "it is
 28 clear from specific facts set forth in the evidence that the Commission has submitted with

1 the Application that immediate and irreparable injury, loss or damage will result if the
2 defendants are notified of the Commission's Application before it is heard." (Doc. No. 3 at
3 1.) The Court, considering the supporting memo and evidentiary record, was satisfied with
4 this argument, and that is why it agreed to accept the SEC's TRO application on an *ex parte*
5 basis, depriving Defendants of the opportunity to be heard up front. The Defendants' first
6 objection to the TRO is therefore **OVERRULED**.

7 **II. Likelihood of Success on the Merits**

8 Defendants' second argument is that the SEC failed to show a likelihood of success
9 on the merits by failing to show that the general partnership interests at issue in this case are
10 in fact securities.

11 The securities laws regulate securities, which are defined to include "investment
12 contracts." 15 U.S.C. § 78c(a)(10). The Supreme Court, in *SEC v. W.J. Howey Co.*, defined
13 an investment contract as "a contract, transaction or scheme whereby a person (1) invests
14 his money in (2) a common enterprise and is led to (3) expect profits solely from the efforts
15 of the promoter or a third party." 328 U.S. 293, 298–99 (1946). The Ninth Circuit has held,
16 moreover, that "solely" in the third prong isn't to be read literally. Rather, the question is
17 whether "the efforts made by those other than the investor are the undeniably significant
18 ones, those essential managerial efforts which affect the failure or success of the
19 enterprise." *SEC v. Glenn W. Turner Enters., Inc.*, 474 F.2d 476, 482 (9th Cir. 1973).

20 In this case, as in most, the determinative prong is the third: Do the investors who
21 purchase the general partnership interests expect profits solely from Defendants' efforts?
22 The leading case on this issue, followed by the Ninth Circuit, is *Williamson v. Tucker*. See

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1 *Koch v. Hawkins*, 928 F.2d 1471, 1476–78 (9th Cir. 1991). In *Williamson*, the Fifth Circuit
 2 held that a general partnership interest can be designated a security

3 if the investor can establish, for example, that (1) an agreement
 4 among the parties leaves so little power in the hands of the
 5 partner or venturer that the arrangement in fact distributes power
 6 as would a limited partnership; or (2) the partner or venturer is
 7 so inexperienced and unknowledgeable in business affairs that
 8 he is incapable of intelligently exercising his partnership or
 venture powers; or (3) the partner or venturer is so dependent
 on some unique entrepreneurial or managerial ability of the
 promoter or manager that he cannot replace the manager of the
 enterprise or otherwise exercise meaningful partnership or
 venture powers.

9 645 F.2d at 424.

10 The SEC addressed the *Williamson* factors at length in its TRO memo, with
 11 substantial reference to a thick evidentiary record. (Doc. No. 3-1 at 14–17.) The Court
 12 found it likely that the SEC could show the general partnership interests at issue in this case
 13 are securities, and therefore subject to the SEC’s regulatory and enforcement powers. The
 14 Court isn’t moved from that finding after having read and considered Defendants’ motion to
 15 dissolve the TRO. For example, Defendants’ first substantive move is to reference the
 16 General Partnership Agreement to claim that, in fact, “[t]here are no limited partners” and
 17 “[a]ll partners are general partners.” Doc. No. 14 at 9. But that technical point misses the
 18 first principle that the term “investment contract,” as defined by the Supreme Court in *W.J.*
 19 *Howey Co.*, “embodies a flexible rather than a static principle, one that is capable of
 20 adaptation to meet the countless and variable schemes devised by those who seek the use
 21 of the money of others on the promise of profits.” 328 U.S. at 299. Thus, the formal
 22 structure or label of the general partnerships doesn’t determine whether they’re securities;
 23 the Court has to consider “the economic realities of the transactions.” Considering that,
 24 Defendants’ second objection to the TRO is **OVERRULED**.

25 **III. Irreparable Harm to Defendants**

26 Defendants take the position that alerting all of their investors of the SEC’s allegations
 27 and the TRO would likely end their business. (Doc. No. 14 at 16–17.) They don’t explain
 28 exactly how this would happen, however, which the SEC is eager to point out. (Doc. No. 18

1 at 6.) Indeed, as the SEC is also eager to point out, Defendants avoid in their motion to
2 dissolve the TRO the SEC's core charge, namely that the price the general partnerships pay
3 for the undeveloped land far exceeds its fair market value. As far as the Court can tell, the
4 Defendants sole come-back to this is that Western did in fact provide detailed disclosures
5 to all investors: "Western provides extremely detailed Partner Representations (attached
6 as Exhibit 3) that fully describe the full extent of the nature and character of the investment,
7 its speculative nature, the unknown time horizon and risks inherent in the investment." (Doc.
8 No. 14 at 15.) One of these representations, on the Court's reading of the document, is that
9 Defendants "will be making a very substantial profit in the sale of the real property to the
10 Partnership. Therefore, as between [Defendants] and [the investor] there exists a conflict
11 of interest and *no* fiduciary relationship." (Doc. No. 14-3 ¶ 74.)

12 This objection is **OVERRULED**, although, out of an abundance of caution for
13 Defendants' interests, the Court will not lift the stay on the receiver's notification obligation
14 until it hears from the parties at the September 17 hearing. The Court remains, it should say,
15 extremely skeptical of Defendants' position—basically, that their investors should not be
16 notified of a public proceeding and public documents that are a part of that proceeding. On
17 the other hand, the SEC's suggestion notwithstanding, the Court doubts that between the
18 time this Order is issued and the time of the September 17 hearing the investors could even
19 be properly notified and make plans to appear in court. This issue, apparently the highest
20 of Defendants' concerns, can wait until Monday.

21 **IV. Conclusion**

22 Defendants' motion to dissolve the TRO is **DENIED**. This denial is **WITHOUT**
23 **PREJUDICE**, of course, to their ability to argue on September 17 that the temporary
24 restraining order should expire without the issuance of a preliminary injunction. The Court

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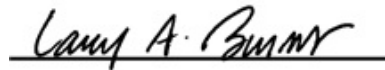
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1 has received Defendants' opposition brief and will give the issues full and fresh
2 consideration.

3 **IT IS SO ORDERED.**

4 DATED: September 12, 2012

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6 **HONORABLE LARRY ALAN BURNS**
7 United States District Judge
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